No. 12,055

IN THE

United States Court of Appeals

For the Ninth Circuit

JAMES G. SMYTH, Collector of Internal Revenue of the First Internal Revenue Collection District of California,

Appellant,

vs.

CALIFORNIA STATE AUTOMOBILE ASSOCIATION (a corporation),

Appellee.

Upon Appeal from the United States District Court for the Northern District of California.

BRIEF FOR APPELLEE.

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BRIEF FOR APPELLEE.

STATEMENT.

The first paragraph under the heading "Statement" on page 3 of appellant's brief appears to be somewhat misleading in saying that "The District Court found the facts substantially as follows (R. 80-86)", inasmuch as the only facts then set forth were that appellee was organized under the laws of California in 1907 as a non-profit corporation, followed by an

enumeration of the purposes for which appellee was so organized, and the finding of the District Court that appellee provided seven enumerated services. The "Statement" then states that the District Court concluded (R. 87) that the "Association is and was at all times here pertinent a club within the meaning of Section 101(9) of the Internal Revenue Code," and (R. 89) "was organized and operated exclusively for pleasure, recreation and other non-profitable purposes during the years 1943 and 1944". The final paragraph recited that judgment was rendered in favor of taxpayer in the amount claimed, with interest, for the years 1943 and 1944.

Actually, "the facts" found by the District Court included also, among others, the following pertinent and important findings (R. 81-86):

> "That Plaintiff at all times since the inception of Federal income taxation in 1913 had been exempt from the imposition of any Federal income and/or excess profits tax until it was finally advised by the Commissioner of Internal Revenue in a letter dated July 27, 1945, that further exemption was denied.
>
> "That the purposes of the Plaintiff have been practically unchanged since its organization and at all times pertinent herein was substantially as follows: to promote and encourage highway construction, improvement, betterment, maintenance and marking for the guidance and warning of the users; to urge adoption of just and intelligent legislation on the use of highways and the regulation of traffic thereon; to maintain offices for col-

lecting and disseminating information and the furnishing of advice and assistance to the owners of automobiles; to protect the legitimate interests of its members in connection with its purposes; to affiliate and associate with similar organizations. None of the foregoing or any other purposes of Plaintiff were designed or intended to make a profit.

"That the Plaiintiff has only the powers necessary to carry out its purposes. The Plaintiff has no power to distributte or set aside any portion of its net income to its members or to any other person except to carry out its purposes.

"That the sum total of the activities of the Plaintiff is designed to alleviate the occasional hardships and inconveniences which are connected with the ownership and operation of pleasure automobiles, and the services rendered by Plaintiff are for the pleasure and recreation of its members.

"That in addition to the normal activities and services of the Plaintiff during the two years here in question, Plaintiff engaged in many activities incidental to the war effort and performed many services for the general public, such as road signing as an official agency of the Federal Government in blackout and dimout areas, services in connection with gas rationing, information and advice furnished members of the armed forces, training of drivers for the Red Cross and other volunteer war services, and in arrangements of reservations and accommodations for its members.

"That none of the normal activities or the wartime activities of the Plaintiff were conducted for

the purpose of earning a profit or accumulating a surplus, nor was any profit derived from any of these activities.

"It has been the policy of the Plaintiff to expend on services all its annual receipts, and during 1943 and 1944 it was prevented from so doing only by reason of wartime restrictions. That in the 16-year period from and including 1931 to 1946 the Plaintiff has had a deficit in 8 years and a surplus in 8 other years.

"That the Plaintiff has never distributed, set aside, or credited on its books by way of dividends or from its earnings any money to any of its members as an incident of their membership in the Plaintiff association. That there has never been any intention to distribute any net income direct to the members. That the directors of Plaintiff serve without financial remuneration.

"That the members of the Plaintiff association collectively defray all its expenses by the payment of identical membership fees and dues.

"That the Plaintiff is a continuing organization whose members make common cause both in a financial sense and in carrying out its stated purposes by group activity as well as by individual action.

"That Plaintiff has annual meetings of its members, meetings of its board of directors, and other meetings occasionally called by the Plaintiff and its standing committees, which meetings members are entitled to attend. Other than these meetings the Plaintiff has no social features. Membership is open to all owners of automobiles unless

they are considered too old, have a bad traffic record, or are otherwise irresponsible. No social, racial or religious discrimination is made with respect to membership. No memberships in Plaintiff are held by any other associations, clubs or organizations. No memberships in Plaintiff association are held by operators of trucks or commercial motor vehicles as such.

"That Plaintiff association is now and at all times pertinent hereto was certified as a 'Motor Club' by the State of California.

"That Plaintiff association is a club.

"That Plaintiff association is a separate and distinct organization from the California State Automobile Association Inter-Insurance Bureau. Although Plaintiff and said Bureau jointly occupy the office quarters of Plaintiff association, said Bureau compensates Plaintiff for the space the former occupies, on a square foot basis, and Plaintiff derives no profit or earnings from its relationship with said Bureau."

It is also pertinent to note that in describing appellee's Magazine Department under (7) on page 4 of his brief, appellant omitted the following from the trial Court's finding: "There is no sale or public distribution of said magazine".

The conclusions of law adopted by the District Court follow (R. 87-89):

"A club is an association the expenses of which are shared among its members. Equivalence between the proportion of a member's contributions and the benefits which he enjoys is of no moment

as long as there is payment by him for the repeated use of its facilities available to the members. Plaintiff is such an association.

"To constitute a club within the meaning of Section 101(9) of the Internal Revenue Code it is not necessary that its activities include social features or a commingling of the members, one with another, in felowship, but it is sufficient if its members make a common cause in a financial or other sense, or if there is present group activity. Plaintiff meets these requirements.

"Plaintiff association is and was at all times here pertinent a club within the meaning of Section 101(9) of the Internal Revenue Code.

"A club operated for pleasure or recreation is one in which the members carry out or enjoy those common purposes acting either individually or collectively. Plaintiff association is such a club.

"Specific activities and services of Plaintiff which if performed by others might be deemed of a commercial or profitable nature are, as carried on by Plaintiff, performed for purposes of pleasure and recreation of its members and not for profit.

"The mere receipt of money, by an organization exempt under Section 101(9) of the Internal Revenue Code, as a result of incidental activities, or in insignificant amounts, is not sufficient to destroy the exemption under that Section so long as the money is expended for exempt purposes. It is the destination and not the source of the income which governs the right to exemption.

"The Plaintiff association was not organized or operated for the purpose of making a profit or

building up a surplus for the benefit of itself or its members.

"Neither the pleasure and recreation nor the non-profitable nature of Plaintiff's objectives and purposes is destroyed by its members' occasional use of its facilities and services for their individual business purposes.

"The excess of receipts over expenditures of Plaintiff association resulting from the unavoidable curtailment of Plaintiff's services during any year did not constitute 'net earnings' within the meaning of Section 101(9) of the Internal Revenue Code, and did not inure to the benefit of any member of Plaintiff.

"Non-profitable purposes within the meaning of Section 101(9) of the Internal Revenue Code are not changed to profitable purposes by the mere fact that in some years the receipts of Plaintiff exceeded its expenditures.

"Plaintiff association was organized and operated exclusively for pleasure, recreation and other non-profitable purposes during the years 1943 and 1944.

"No part of the net earnings of Plaintiff association inured to the benefit of any of its members during the years 1943 and 1944.

"Plaintiff is entitled to judgment as prayed."

It may be noted at this point that after the submission by appellee to the District Court of proposed findings of fact and conclusions of law, no objections thereto or suggestions for change in any respect were filed by the Government in opposition to such proposed findings or conclusions.

SUMMARY OF ARGUMENT.

Appellee was at all times, including the years 1943 and 1944, a "club" within the meaning of Section 101(9) of the Internal Revenue Code, as well as under the practically identical provisions of all Revenue Acts beginning with that of 1916, down to date. In a club of this nature, and in this particular club, neither social intercourse nor commingling of members is necessary, although, as will later be shown, there was commingling of members in annual meetings, periodical meetings of its board of directors, and in connection with the meetings and activities of ten standing committees, etc. (R. 178.) Appellee comes squarely within a number of definitions, which will be cited herein, of the term "club". Appellee also meets the terms of the statute that it be organized and operated exclusively for pleasure, recreation, and other non-profitable purposes, and that no part of its net earnings inures to the benefit of any member.

The District Court, in separate findings, has held that appellee meets all the requirements of Section 101(9).

A. HISTORY OF SECTION 101 (9) OF THE INTERNAL REVENUE CODE.

The section in question during the years 1943 and 1944, as well as prior and subsequent thereto, provided as follows:

"Section 101. EXEMPTIONS FROM TAX ON CORPORATIONS.

"The following organizations shall be exempt from taxation under this chapter—

* * * * * * *

"(9) Clubs organized and operated exclusively for pleasure, recreation, and other nonprofitable purposes, no part of the net earnings of which inures to the benefit of any private shareholder."

The Revenue Act of 1913 was the first Income Tax Act under the 16th Amendment, but it provided that the income tax should not apply to:

"* * * any corporation or association organized and operated exclusively for religious, charitable, scientific, or educational purposes, no part of the net income of which inures to the benefit of any private stockholder or individual, nor to business leagues, nor to chambers of commerce or boards of trade, not organized for profit or no part of the net income of which inures to the benefit of the private stockholder or individual; nor to any civic league or organization not organized for profit, but operated exclusively for the promotion of social welfare; * * *."

The foregoing exclusions of the 1913 Act did not specifically include a club of the type of appellee, but in spite of that fact, the Commissioner of Internal Revenue did not impose any income tax upon appellee under that Act.

Section 11(a) of the Revenue Act of 1916, which was the next Revenue Act after that of 1913, provided exemption from income tax of:

> "Ninth. Clubs organized and operated exclusively for pleasure, recreation, and other nonprofitable purposes, no part of the net income of which inures to the benefit of any private stockholder or member."

It will readily be observed that, except for the change of several unimportant words in the section just quoted, the same provision of law has continued to grant exemption to the clubs described from 1916 down to the present time.

Identical language to that of the 1916 Act was contained in the Revenue Act of 1918, and such exemption was provided in the Revenue Act of 1921 in the same language.

The Revenue Act of 1924, Section 231(9), gave the same exemption but changed the wording very slightly from "private stockholder or member" to "private shareholder", as it is today.

The same identical language as used in the 1924 Act, providing income tax exemption to such clubs, is found in each subsequent Federal Revenue Act to and including the Revenue Act of 1938, and identical wording is found in the present codification of revenue laws called the Internal Revenue Code. In fact the exempting provision has been enacted by Congress eleven times.

Throughout its existence, since the inception of the income tax in 1913 down to the year 1943, appellee had never been required by the Federal Government to pay, nor had it paid, any income or excess profits

taxes. It was, therefore, considered by the Government to be exempt from taxation for a period of thirty (30) years, and the Commisioner of Internal Revenue did not seek to subject it to taxation until his first ruling letter to that effect, dated September 23, 1944 (Exhibit 1-B).

B. APPELLEE IS A "CLUB" WITHIN THE MEANING OF SECTION 101(9) OF THE INTERNAL REVENUE CODE.

The New International Encyclopedia, Volume 5, pages 487 et seq., defines the word "club" as follows:

> "A word said to be derived from the Saxon cleofan, to divide—a club being an association the expenses of which are shared among the members."
>
> "*The Automobile Club of America,* devoted to the advancement and regulation of motoring was established in 1890 and has 1,660 members. *The Aero Club of America,* founded in 1906 for the promotion of aeronautics, now has 340 members." (Italics supplied.)

It is important to note that the foregoing definition cites *The Automobile Club of America* as its first illustration of a "club".

The following judicial construction of the term "club" is pertinent and illuminating:

> "The subdivision of lake frontage land, under which purchasers of lots were to have common or community rights to lake frontage bathing and boating privileges, and water supply, was held a violation of covenants prohibiting its use for

'club' purposes; a 'club' meaning a combination or association formed to combine the operation of persons interested in the promotion or prosecution of some object, and as used in the covenant, including clubs of all kinds."

Robert v. Gerber, 202 N. W. 701, 703, 187 Wis. 282.

"A club is an association of individuals for pleasure or profit."

Martin v. State, 59 Ala. 34.

"The word 'club' has no very definite meaning. Clubs are formed for all sorts of purposes, and then in no uniformity in their constitution and rules."

Commonwealth v. Pomphret, 137 Mass. 564, 567.

Webster's New International Dictionary sets forth, among other definitions of the word "club," the following:

"To unite for a common end, or contribute to a common stock; as to club exertions. * * *"

Intransitive—"to form a club; to combine for the promotion of some common object; to unite."

Webster's same dictionary, Second Edition, Unabridged, in defining the word "association" gives the following synonyms:

"company, fellowship, body, league—association, society, *club*—agree in the idea of *a body of persons united in the interest of a common object.* Association and society are practically interchangeable, the Young Men's Christian Associa-

> tion, the Christian Endeavor Society, The American Historical Association, The Philological Society. Frequently, however, association suggests a somewhat larger inclusiveness than society, whether with regard to the objects of the organization or to the persons admitted to membership. A club is usually a more private body than either of the others and is often purely social." (Italics supplied.)

The Commissioner of Internal Revenue himself, in letters addressed to appellee, dated January 25, 1945, and August 21, 1945 (Exhibits 2-A and 2-C), dealing with the capital stock tax returns of appellee for the years ending June 30, 1944, and June 30, 1943, respectively, refers to the former bureau rulings of September 23, 1944 (Exhibit 1-E), and July 27, 1945 (Exhibit 1-G), that appellee would be required to file returns of income, and twice uses the expression:

> "* * * *that automobile clubs such as yours,* which are within the scope of the Bureau rulings, will not be required to file returns of income for years beginning prior to January 1, 1943." (Italics supplied.)

Those two letters not only plainly characterize appellee as an *automobile club,* but are also directly connected with the rulings of the Commissioner with reference to filing income tax returns, as they specifically refer to such rulings.

The foregoing rulings, Exhibits 2-A and 2-C, are pertinent for the further reason that a capital stock tax was due in 1943 and 1944 only if a corporation was

subject to the income tax, and if a corporation was exempt from income tax it was then also exempt from the capital stock tax. Section 1201 of the Internal Revenue Code demonstrates this point. It read as follows, before its elimination from the code as to years ending after June 30, 1945:

> "(a) The taxes imposed by Section 1200 shall not apply—
>
> "(1) CORPORATIONS EXEMPT FROM INCOME TAX —to any corporation enumerated in Section 101; * * *"

Likewise, an excess profits tax was payable in 1943 and 1944 only if a corporation was subject to income tax.

Furthermore, in the final ruling of the Commissioner of Internal Revenue himself, in a letter dated July 27, 1945, to appellee (Exhibit 1-G), the Commissioner refers to "automobile clubs" in the following language:

> "Prior to the time that the information submitted by you in 1941, was taken up for consideration a substantial number of *automobile clubs* had been held to be entitled to exemption under Section 101(9) of the Internal Revenue Code and prior revenue acts. While the information submitted by you was under consideration in this office, it was decided to reexamine the general question of whether *an automobile club or association* having the usual purposes and activities is entitled to the exemption provided in Section 101(9) in connection with a particular case, and in G.C.M. 23688 (C.B. 1943, 283) it was con-

> cluded for the reasons therein stated that the subject automobile association is not entitled to the exemption. * * *'' (Italics supplied.)

Thus the Commissioner has a number of times called appellee itself, as well as similar organizations, an "automobile club".

In *Portland Cooperative Labor Temple Association v. Commissioner of Internal Revenue,* 39 B.T.A. 450, petitioner contended that it was exempt from income and excess profits taxes under Section 101(1) granting exemption to labor, agricultural and horticultural organizations. Speaking of the term "labor organization", the Board said:

> "The term has been used continuously for 30 years to bestow tax exemption, and it never has been found desirable by Congress to qualify it or by the administrator to give it a narrowing interpretation. There is no occasion to attempt a definition now. It bespeaks a liberal construction to embrace the common acceptation of the term, including labor unions and councils and the groups which are ordinarily organized to protect and promote the interests of labor. The petitioner, we think, was within such a category during the years 1934 and 1935, and was therefore exempt from tax."

On page 7 of appellant's brief, in support of its contention that appellee is not a club, the following statement appears:

> "In the absence of a statutory definition or helpful legislative history it seems appropriate to

> conclude that Congress intended by the section to exempt organizations which are usually and commonly referred to as clubs."

While the criterion suggested by the Government in the language just quoted is by no means exclusive, as is indicated by the definitions of the term "club", *infra,* appellant has apparently unwittingly added strength to appellee's contention by referring to *exempt* organizations which are *usually and commonly referred to as clubs,* in view of the fact that as a matter of common knowledge the term "automobile club" is quite universally used to describe an organization such as appellee. Many of them actually have the word "club" included within their official names, such as the Automobile Club of Southern California.

Also in the definitions of the word "club" on the same page of appellant's brief there is reference in each definition to the promotion or pursuance of some common object. There can, we believe, be no denial of the statement that the members of taxpayer were banded together for the promotion of the objectives set forth in the findings of fact of the District Court (R. 82-84), which collectively clearly constitute a "common object".

The definitions from Webster's New International Dictionary and from Funk and Wagnalls' New Standard Dictionary quoted by appellant on page 7 of his brief define the word "club" in a manner which is helpful to appellee. Certainly the appellee is "an association of persons for the promotion of some

common object * * *'' or objects, being those objects and purposes described in detail, *infra.* The further definition that membership in a club is ''usually'' conferred by ballot certainly does not preclude the existence of a club in which membership is not so conferred. For example, in G.C.M. 22116, C.B. 1940-2, page 100, granting exemption to a college alumni association under Section 101(9), membership in the association was not limited in number and the members were not selected by ballot. Anyone who received a degree from the college or who was in any way connected with the college even though not the recipient of a degree, was eligible for membership upon payment of regular annual dues. This ruling is still in effect and clearly shows that even the Bureau of Internal Revenue does not adhere to the argument made in the Government's brief in construing the statute.

In addition, in O.D. 280, C.B. 1919, page 203, the Bureau of Internal Revenue held that a political club was exempt under this same statute. That ruling is still in effect and likewise clearly shows that the Bureau has never imposed the requirements of limited membership or membership conferred by ballot as a requirement for exemption.

Furthermore, other and more numerous dictionary definitions, as well as judicial definitions of the term ''club'', which have hereinbefore been cited in support of appellee's contention that it is a club, do not lay down any such conditions as set forth in appellant's brief.

The District Court has found as a fact "That Plaintiff association is a club" (R. 86).

Appellant's statement on page 8 that appellee has no clubhouse or other meeting place is not in accord with the facts as appellee not only must have a place for its annual meetings, but also has a large headquarters building at 150 Van Ness Avenue, San Francisco, together with thirty-five (35) branch offices scattered throughout the territory which it serves. Members not only can, but do, meet and particularly at its headquarters, where its Board of Directors and its numerous committees meet both periodically and specially for the transaction of business in the interest of the entire membership.

Also on page 8 of its brief, appellant pointed out that the Court below concluded that (R. 87) "A club is an association the expenses of which are shared among its members," and also concluded that (R. 87) "To constitute a club within the meaning of Section 101(9) of the Internal Revenue Code it is not necessary that its activities include social features or a commingling of the members, one with another, in fellowship, but it is sufficient if its members make a common cause in a financial or other sense, or if there is present group activity." In its last quotation appellant omitted the final sentence of the District Court's conclusion, which reads "Plaintiff meets these requirements."

Appellant then says that he finds no support for the conclusion that the mere sharing of expenses among

individuals gives to the group the aspect of a club, but he fails to take into account the conclusion of the Court below, just above quoted, which obviously expands the Court's preceding finding that "A club is an association the expenses of which are shared among its members," and furnishes additional reasons for the Court's ultimate conclusion that appellee is a club.

Appellant admits on page 8 of his brief that the use of the word "club" does not *necessarily* carry with it the idea of social intercourse. That is exactly what appellee contends and what the Court below has found (R. 87).

It is observed that there are two quite important omissions on page 9 of appellant's brief where it is said that "It is difficult to understand what the lower Court had in mind by saying that 'it is sufficient if its members make a common cause in a financial * * * sense' " (R. 87). That excerpt is taken from Conclusion II just above referred to (R. 87), which appears on page 8 of appellant's brief, and while only the two words "or other" are omitted where the three asterisks appear, it is obvious that such omission restricts the meaning of the lower Court's conclusion in a manner which was clearly not intended by that Court. The words "or other" cover the numerous ways in which the members of a club under Section 101(9) operate as a club, and naturally include the variety of other activities of the appellee which collectively, in the judgment of the lower Court, qualify it as a club. It would seem that nothing was to be

gained by the omission of the two words "or other" and the substitution therefor of the three asterisks, except to provide a basis for an argument that taxpayer could not be a club if its members merely make a common cause in a financial sense. The lower Court did not so restrict its findings.

The other noteworthy omission by appellant is the phrase "or if there is present group activity" which immediately, and as part of the same sentence, follows "in a financial or other sense". To all this should be added the concluding sentence used by the Court, "Plaintiff meets these requirements."

Appellant did not indicate that another phrase followed the word "sense" in his quotation on page 9 of his brief, and that another complete sentence was also omitted. The result has been to distort both the content and the meaning of the District Court's conclusion.

Appellant is completely in error in several assertions he has made in the second paragraph on page 9 of his brief, especially where he says that "The entire record clearly shows that taxpayer has no activities commonly associated with club functions," and that if a motorist thinks about joining an association of the type of appellee "his first and only consideration is whether or not the services and reduced insurance rates are worth the dues he will be required to pay". It is believed that the first statement above quoted is completely refuted by "the entire record" to which appellant refers, and the findings of the lower Court

which show that appellee has an organization typical of many clubs in that it has executive officers, a board of directors, a considerable number (ten) of functioning committees, a dues-paying membership, annual meetings which all members are invited to attend, pursuit of a common objective, etc. The second quoted statement of appellant is likewise refuted by the record, including the finding of the lower Court that appellee is a separate and distinct organization from the California State Automobile Association Inter-Insurance Bureau (R. 86); that appellee does not and never has maintained or operated an insurance bureau, department or other agency for the placing of automobile insurance; that the right to obtain insurance through the Inter-Insurance Bureau is not open to all members of appellee, but is restricted to selected individuals who must meet certain qualifications and who are not entitled to so obtain insurance if they have a record of hazardous driving, a bad insurance record, etc. Furthermore, appellee's members are not required to become subscribers of the Inter-Insurance Bureau (R. 126, 127, 140, 141, 183). In addition, there is no certainty that insurance will cost an insured under the Inter-Insurance Bureau less than it would in non-board or conference companies, or in other cooperative insurance concerns (R. 141).

On pages 10, 11 and 12 of appellant's brief there are quotations from and discussion of G.C.M. 23688, 1943 C.B. 283, a memorandum issued by the chief counsel of the Bureau of Internal Revenue, which memorandum overrules or modifies a number of other rulings of

many years' standing. The subject of discussion in that memorandum is obviously a *nation-wide federation of automobile clubs,* as is evident from the last two paragraphs on page 1 thereof, where the M Association is stated to function to a large extent as a "federation of automobile clubs" and as "the managing agency of several local automobile clubs," and referring also to the fact that membership in that club is confined to "(a) State Associations, (b) automobile clubs, (c) automobile divisions, (d) commercial vehicle organizations." Although the Bureau of Internal Revenue, in conformity with its consistent practice uses merely a letter to identify the "M Association", the foregoing description points strongly to the assumption that the subject of the memorandum is the American Automobile Association.

And on page 2 of said memorandum we find that "individuals who are, or become,, affiliated with this corporation *shall not be members,* but shall be classed as regular and honorary associates * * *." (Italics supplied.)

The M Association is wholly unlike appellee, as the latter, whose activities are set out in the present record, does not function as a federation of automobile clubs or as a managing agency of local automobile clubs, nor does it conduct or participate in any such functions. Likewise, it does not organize, supervise, or grant affiliation to other corporations, associations, or organizations with similar objects and purposes, as described in paragraph (f) of the by-laws of M Association. Appellee has no member clubs and does not

in any sense operate as a federation of automobile clubs.

Appellee is sharply distinguished from the M Association also in that it bears no resemblance whatsoever to the organization described in G.C.M. 23688, whereby "Arrangements have also been made with certain merchants in one area whereby members of one of the local organizations may purchase clothing, laundry, furniture, and automobile supplies at less than the usual selling prices of such articles." Appellee does none of these things (R. 175).

Another difference between appellee and the M Association is that in the latter, individual members as such have no right to vote in the affairs of the corporation (page 2, paragraph 4), whereas in appellee the individual members have both of such rights, and the record shows that they do vote and otherwise actively participate in the affairs of the corporation. Likewise, appellee, unlike the M Association, does consist of members who participate in activities looking to the rendition of the services offered by appellee, all of which are designed to and do contribute to the pleasure and recreation of the membership.

Again, there is a radical difference between appellee and the M Association, which latter is stated in G.C.M. 23688 to operate "in the nature of a non-profit cooperative buying association," as appellee indulges in no such activities whatever. Furthermore, appellee is not itself, nor does it perform any of the functions of, a "commercial vehicle organization", as does the M Association.

A comparison of the activities and operations of appellee and M Association show it to be widely divergent from the latter in practically every respect.

The record indicates either affirmatively as to certain activities of appellee, or negatively as to others, that appellee did not engage in a number of the activities attributed to the M Association.

In this connection attention is invited to the admission of appellant that appellee "did everything that is in the record here that they did do, and did nothing else" (R. 175). (Italics supplied.)

The great differences between appellee's activities, as shown by the record, and the activities and purposes of the M Association as shown in G.C.M. 23688, infra, weaken materially the force of the Commissioner's final ruling of July 27, 1945, Exhibit 1-G (R. 17), in which it is stated that "in G.C.M. 23688 (C.B. 1943, 283) it was concluded for the reasons therein stated that the subject automobile association is not entitled to the exemption. This opinion was first published during the first part of July, 1943, after which the information submitted by you during October, 1941, was again taken up for consideration *in the light of the view expressed in that General Counsel's Memorandum,* and it was concluded with the concurrence of the chief counsel and the approval of the then acting secretary of the treasury, that you are not entitled to the exemption provided in Section 101(9) * * *." It is submitted that G.C.M. 23688 has no proper application to the case at bar. (Italics supplied.)

It is also quite interesting to note that the same chief counsel of the Bureau of Internal Revenue, J. P. Wenchel, who issued G.C.M. 23688, infra, also issued G.C.M. 22116, 1940-2, CB 100, infra, holding that the M Alumni Association was exempt from tax under Section 101(9) of the Code. It was stated to be organized primarily to promote in every proper way the interests of the M College and to foster among its graduates a sentiment of regard for each other and attachment to their alma mater. The purposes of M Alumni Association included the following: "To raise money by subscriptions, and to grant any rights and privileges to subscribers." The chief counsel stated that "Other income is derived from the sale of advertising space in the magazine and a small amount of interest is received from a fund composed of paid life membership fees. The income is used to defray operating expenses of the association, and any balance over expenses is given annually to the college to be applied to some need." No mention whatever is made of any pleasure or recreation purposes, nevertheless exemption from income taxation under Section 101(9) of the Code was granted.

In I.T. 2693, XII-1 C.B. 59, income tax exemption was allowed a club incorporated with the declared purpose of making trails and roads in certain mountains, to erect camps and shelter houses therein, to furnish maps and guide books, and to make these mountains play a larger part in the life of the people. Its income is from dues and the sale of maps, guide books and similar publications and no part inures to the benefit

of any private individual. This ruling was based upon the same reasoning as that upon which some of the earlier automobile club rulings were predicated, but revoked in G.C.M. 23688, infra, but I.T. 2693 has not been revoked or rescinded and apparently therefore still stands.

Appellant says that appellee association does not provide for commingling of members in fellowship and hence is not a club. It apparently bases such assertion upon some of the language dealing specifically with the excise tax, under Section 1710 of the Code, imposed on a "social, athletic, or sporting club or organization," and applicable only to that type of club and not to clubs mentioned in Section 101(9). Such commingling is not required as an element in the definition of a club under the latter section, or under the regulations issued in connection therewith.

We cannot agree with appellant's statement on page 8 of his brief implying that a club must have a clubhouse. It is a far stretch of credulity to suppose that Congress intended the tax exemption under Section 101(9) to turn upon the kind of physical facilities possessed by the organization.

The Commissioner's final adverse ruling of July 27, 1945 (Exhibit 1-G) (R. 15) shows that such ruling was largely predicated upon G.C.M. 23688, infra, which we submit has no proper application, and upon the assertion that appellee was not a club under the decision in *Arner v. Rogan,* cited and discussed in G.C.M. 23688, and on pages 10, 11 and 12 of appellant's brief.

Arner v. Rogan dealt with the question of the application of the *excise* tax under Section 501 of the Revenue Act of 1926 to a *social, athletic or sporting club,* and not to the exemption from *income* tax of a club such as taxpayer under Section 101(9) of the Code. Section 501 of the Revenue Act of 1926 was the predecessor and counterpart of Section 1710 of the Internal Revenue Code, which is found under Chapter 10, *Admissions and Dues,* while Section 101(9) is found in Chapter 1, *Income Tax.*

Section 1710 *imposes* an *excise* tax upon dues and membership fees of a specifically described type of club, wholly unlike the clubs described in Section 101(9), which section *exempts* the same from *income* tax.

There is, therefore, in the tax treatment of the divergent types of clubs respectively dealt with in Sections 1710 and 101(9) no necessary or natural connection, and the descriptions of these two distinctive groups of clubs add further emphasis to the fact that the two sections of the Code mentioned are not only not identical, either in description or purpose, but that the only thing they have in common is the generic term "club".

There is no reference whatever in Section 101(9) to social, athletic, or sporting clubs, which are the sole objects of taxation under Section 1710, and it is obvious from the most cursory consideration of the terms "pleasure" and "recreation" that certain forms of both pleasure and recreation may be indulged in by

persons acting individually and with no association whatever with other individuals.

In *Better Business Bureau v. United States,* 326 U. S. 279, the Supreme Court carefully noted that Congress has written a slightly different definition into the Social Security Act than in the Income Tax Act, and said that this indicates an intention on the part of Congress to make a demarcation between certain types of corporations. The same reasoning applies to the distinction made by Congress by defining, in Section 101(9), clubs organized and operated exclusively for pleasure, recreation and other non-profitable purposes, as distinguished from social, athletic or sporting clubs, which are required to pay an excise tax under 1710 of the Code.

The pertinent language of the Supreme Court in this connection follows:

> "* * * And Congress had made it clear, from its committee reports, that it meant to include within Section 811(b) (8) only those organizations exempt from the income tax under Section 101(6). Significantly, however, Congress did not write into the Social Security Act certain other exemptions embodied in the income tax provisions, especially the exemption in Section 101(7) of 'business leagues, chambers of commerce, real estate boards, or boards of trade'. Petitioner closely resembles such organizations and has, indeed, secured an exemption from the income tax under Section 101(7) as a business league. Thus Congress had made, *for income tax exemption purposes,* an unmistakable demarcation between corporations or-

> ganized and operated exclusively for educational purposes and those organizations in the nature of business leagues and the like. Its manifest desire to include only the former within the meaning of Section 811(b) (8) of the Social Security Act prevents us from construing the language of that section to include an organization like petitioner. * * *" (Italics supplied.)

Referring to the quotation in G.C.M. 23688, infra, from *Arner v. Rogan* by appellant on page 11 of his brief:

> "* * * at least there must be some sort of association or cooperation between the members in an effort to reach some common objective before we may consider that there is a club or organization,"

it may be stated, unequivocally, that as the record shows, there is both association and cooperation between the members of appellee "in an effort to reach some common objective," so that in fact the quotation from *Arner v. Rogan,* upon which appellant relies, is in support of appellee's contention. The whole purpose of the organization and operation of appellee was to provide the necessary association and cooperation among its members for the achievement of its objective, namely, the pleasure and recreation of the passenger car owners constituting its membership, by the improvement and marking of roads, obtaining legislation to further the construction of more and better highways, providing a quick and efficient towing service to members in distress on the highways, furnishing travel information and guides to its members, etc.

Quite significantly the Court also said in *Arner v. Rogan:*

> "*There never was any general corporate meeting of any kind and one man seemed to determine all questions even without reference to a Board of Directors* and apparently without any express authority to do so. The only evidence of any intention to give members any control is contained in the various pieces of literature which were apparently handed out by the manager, or sent out by the manager, and, according to his testimony, the only purpose thereof was advertising. The evidence shows that *members never met together or in committee* and *never participated in any activities which are normally carried on by members of clubs* or similar organizations, nor is there evidence that the patrons were *entitled* by the terms of their contracts to so participate." (Italics supplied.)

It may be pertinent again to point out that the members of appellee association, through collective action, regularly elect a board of directors, made up of twenty-one members of the association, which meets both regularly and specially throughout the year. It has ten committees, enumerated in the record, and to which a considerable number of members, in the aggregate, are appointed. Other members of appellee attend special committee meetings, such as those of the legislative committee, although not members of that committee. The members of appellee are invited and urged to and do attend and participate in the annual meetings of the association. All of the committee work and other activities are designed to further, through asso-

ciation and cooperation among the members, the common objectives of appellee, which obviously could not be achieved except through such collective action. Appellee therefore meets the very requirements laid down by the Court in *Arner v. Rogan*.

It is significant to note that while the section of the regulations issued by the Commissioner under Section 101(9) bears the title "Social Clubs", it is *not* restricted to such clubs, but specifically provides that in addition thereto the exemption granted by Section 101(9) applies to practically all recreation clubs supported by membership fees, dues, and assessments.

Of special significance is the fact that under the regulations promulgated under the various revenue acts preceding the establishment of the Internal Revenue Code, as well as the similar section under the code itself—Section 101(9)—the article or section of such regulations has been headed "Social Clubs", obviously for the purpose of brevity, although from the context of the regulations, beginning with those under the Revenue Act of 1916 (Regulations 33), it is quite clear that recreation clubs supported by membership fees, dues and assessments (as is the appellee), are included in the exemption along with so-called social clubs. It could not be otherwise, in fact, as the regulations can only carry out the intent of Congress in defining the types of clubs to be granted exemption, and cannot restrict the types so enumerated. The first regulations on the section under discussion are found in Art. 72, Regulations 33, under the Revenue Act of 1916, and read as follows:

> "Social Clubs. Social clubs organized and operated exclusively for pleasure, recreation, and other non-profitable purposes are exempt from the tax, provided no part of any net income which they receive inures to the benefit of any private stockholder or individual. This exemption will reach practically all social and recreation clubs which are supported by membership fees, dues, and assessments."

However, under Art. 520 of Regulations 45, under the Revenue Act of 1918, the context did not stress social clubs as it did under Regulations 33, *supra,* but reads: "The exemption applies to practically all social and recreation clubs * * *," which terminology has been carried throughout the regulations under the various legislative provisions in the Revenue Acts and the code dealing with the exemption here under consideration, and the latest regulations under Section 101(9)—Regulations 111, Section 19. 101(9)—provide as follows:

> "Social Clubs. The exemption granted by Section 101(9) applies to practically all social and recreation clubs which are supported by membership fees, dues, and assessments. If a club engaged in traffic, in agriculture or horticulture, or in the sale of real estate, timber, etc., for profit, such club is not organized and operated exclusively for *pleasure, recreation, or* social purposes. *Generally, an incidental sale of property will not* deprive the club of the exemption." (Italics supplied.)

The regulations have not been changed since 1937, although there have been several reenactments of Sec-

tion 101(9) since then, without change. Therefore, there is no basis in the regulations for the position taken by the Commissioner that appellee is no longer exempt.

In *Bryant v. Commissioner,* 111 Fed. (2d) 9, decided by this Court, and reversing the Board of Tax Appeals, the question was whether interest paid Mrs. Bryant on street improvement bonds of the city of Los Angeles was tax exempt. The administrative practice at least until 1936, or for more than 22 years, was to treat as within the statutory exemption interest upon bonds which were not general obligations of the issuing political subdivision but were payable only out of a particular fund. In 1936, two years after the tax there involved, a contrary opinion was expressed in a general counsel's memorandum. The Court said:

> "*The established administrative practice of so many years, during which time the exemption was several times reenacted, carries weight as a construction of the statute* which is not offset, at least as to the tax year in question, by the later expression of opinion in G.C.M. 16861, XV-2 Cum. Bull. 179 (1936)." (Italics supplied.)

In *Citizens National Trust & Savings Bank of Los Angeles v. United States,* 135 Fed. (2d) 527 (CCA-9), the bank contended that R. S. 3186 gave the United States a lien only upon property possessed by the taxpayer at the time of the distraint and that the lien did not attach to after-acquired property. This Court held that the statute, by its terms, applied to after-acquired property but went on to say that if the statute was so

general in its terms that an administrative interpretation was appropriate, the statute had been interpreted to apply to after-acquired property. Since such interpretation the section had been twice amended with no addition of a definite provision as to after-acquired property and presumably with Congressional knowledge of the departmental interpretation. The Court said: "Therefore, such interpretation must be taken as approved by Congress."

Furthermore, it is of the greatest significance that the Bureau of Internal Revenue for a period of 30 years, from 1913 to 1943, under these very regulations, even though entitled "Social Clubs", consistently exempted appellee from income taxation. Other automobile clubs were also so exempted. G.C.M. 23688, infra. It is clear, therefore, that appellee is not required to qualify as a social club under Section 1710 of the Code in order to entitle it to exemption under Section 101(9).

C. APPELLEE WAS ORGANIZED AND OPERATED EXCLUSIVELY FOR PLEASURE, RECREATION, AND OTHER NONPROFITABLE PURPOSES.

It is important first to determine the full meaning of the words "pleasure" and "recreation", as both words have definitions and synonyms which enlarge the scope of meaning conveyed by the mere words themselves.

Roget's International Thesaurus, in defining the word "pleasure", includes the synonyms, "gratifica-

tion", "enjoyment", "well-being", "satisfaction", "happiness", "joy", "cheerfulness", and "pleasant time".

The same authority in defining the word "recreation" gives the synonyms "amusing", "entertaining", and "diverting".

Webster's dictionary of synonyms for each of the words "pleasure" and "recreation" includes several of those found in Roget.

In *National Surety Company v. Jarrett,* 121 S.E. 291, 295, 95 W. Va. 420, it is said that " 'pleasure' is synonymous with comfort, consolation, contentment, ease, enjoyment, happiness and satisfaction."

In *Committee for Industrial Organization v. Hague,* D.C.N.J., 25 F. Supp. 127, 145, it is stated that "the purpose of most parks is the 'recreation' of the public, including not only physical recreation, but mental recreation, * * *."

It may be somewhat difficult in these days of wide, smooth, well-constructed concrete highways, so amply marked by road signs that an automobile traveler may be kept informed as to his location, the name and distance of the next town or city, where he should make a necessary turn, and even the condition of the highway if a portion farther on is under repair or construction, to project one's thoughts back to the days of 1907 when appellee was first organized, and to 1913 when, as David E. Watkins (secretary and general manager of appellee since that year) testified (R. 148, 149), the condition of the roads was "deplorable",

meaning, what we believe to be a matter of common knowledge, that there were practically no hard-surfaced highways, the roads were usually very narrow, dusty during dry weather, rutted and slippery in wet weather, when it was difficult for two vehicles to pass each other without, in many cases, endangering safety by getting off into a ditch and causing great inconvenience, discomfort and, in many cases, some type of casualty. In 1907 the automobile was new, it had been in even very limited use only for a few years, and was being used practically exclusively for pleasure purposes. The automobiles themselves at that early date were, to some extent, experimental in nature and construction, and were subject to frequent breakdowns on the road, particularly under the highly unfavorable road conditions which then existed.

It was in the light of such an unfavorable state of affairs, which are a matter of common knowledge, that the incorporators of appellee got together to form an organization for the purpose of improving road and other conditions so as to make the use of pleasure cars safer and more enjoyable, thus contributing materially to the "comfort", "contentment", "enjoyment", "satisfaction" and pleasure of their owners, and to further the opportunities for recreation which such improved conditions would provide, including easier and safer access to mountains, lakes and other recreation spots.

Even a cursory glance at the purposes set forth in appellee's Articles of Incorporation on August 30, 1907, will show that they were all designed to promote the pleasure and recreation of its members:

"Throughout the State of California and elsewhere,

To promote the improvement of the highways;

To encourage proper highway maintenance;

To accomplish the proper marking of the highways;

To urge just and rational highway legislation;

To further all good roads projects;

To protect the legitimate interests of members;

To affiliate or associate with itself similar associations;

To promote speed and endurance contests for motor vehicles;

To purchase, hold and convey real and personal property as its purposes may require."
(Ex. 1-A.)

Throughout its history, appellee has adhered to the purposes thus set forth in its articles of incorporation, and its whole plan and purpose has been a constant endeavor to secure the improvement of highways, including the function of road signing, and the other activities set forth in the evidence in this case, so that its members would progressively be furnished with all the aid and assistance which could be made available to contribute to their pleasure and recreation in the use of their pleasure cars. There has been no change in the type of appellee corporation as originally organized.

As the evidence further shows, appellee during the years 1943 and 1944, as well as prior and subsequent

thereto, has furnished, among other services, the following:

Emergency road service, including towing service, for the aid and assistance of its members who may encounter trouble of any kind with their automobiles while on the highways, such service being restricted, however, to passenger cars (R. 123, 124, 128-132).

Claim adjustment service for the convenience and comfort of its members when they were involved in accidents, in adjusting the matter of damages, including adjustments made with municipalities for infractions of traffic regulations, etc. (R. 131, 132).

Investigating, listing and publishing, for the benefit of its membership, the names of accredited hotels, lodges, restaurants, etc., where appellee's members might rely upon obtaining satisfactory and adequate lodging, and meals, thus contributing to their comfort, well-being and pleasure, and relieving them of anxiety as to whether certain stopping places were safe and reliable (R. 167, 168, 198).

The erection, repair and maintenance, at its own expense, with the exception of the actual cost of materials, of road signs, including parking signs, direction signs, distance signs, restriction signs, signs for cities, towns and resorts, and for places of historical interest, as well as signs containing information as to local ordinances and regulations, danger and detour signs, etc. In connection with such road signing, appellee spent large sums of money for which it was not reimbursed. No one else has done such road signing

in appellee's territory since the latter began it in 1914, and appellee started it for the recreational convenience and pleasure of its members (R. 170, 192-194).

Appellee's chief engineer, James W. Johnson, is a member of the Joint Committee on Uniform Traffic Control Devices which holds regular meetings in Washington, D. C., and which designs traffic devices (R. 195).

The publication of a monthly magazine, "Motorland", issued as one of the incidents of membership, without further cost, each month to all the members of appellee to keep them advised not only of the activities of their association but of all matters of interest arising in connection with the operation of their automobiles. While in earlier years appellee had some income from advertising in said magazine, such income was entirely eliminated late in 1941 and there was no such income in 1943 and 1944 (R. 161-164).

The issuance of licenses by appellee's touring bureau under arrangements with the State of California by which a block of licenses each year is assigned to appellee for distribution to its members. Such distribution eliminates the waste of time and inconvenience involved in standing in line at State automobile registration offices and enables appellee's members to obtain their annual licenses with a minimum of inconvenience and discomfort (R. 199).

One of the most important and one of the most widely used of the services offered by appellee to its membership is its touring service. Through its touring

bureau, members obtain a wide variety of information, particularly for use in connection with contemplated trips for pleasure and recreation. A very large number of maps are distributed to appellee's members through the touring bureau, including state and sectional maps, maps of various Western States and highways, strip maps, etc. Lists of hotels, lodgings, and restaurants distributed to its members cover not only the Western United States but the entire country and Canada as well. The touring bureau also furnishes a large volume of information to members planning vacation trips, including places to stay, roads to take, highway conditions, facilities for camping, fishing and hunting conditions, including information as to open and closed seasons, etc. During the past five years, the average number of calls for such information which have been answered by the touring bureau was a minimum of 500,000 inquiries each year (R. 197-201). In that connection, it is interesting to note, as shown on page 25 of the statement attached to appellee's several claims for refund, appellant's Exhibits A and B, that in the year 1940 the report of the president contained a detailed statement of services rendered by its touring bureau, including the furnishing of information to practically 200,000 motor touring parties, preparation of 19,000 transcontinental routings, and 30,000 other out-of-state routings, the issuance of more than 367,000 road maps, and the handling of over 170,000 telephone requests from members seeking travel information, exclusive of thousands of such inquiries received by San Francisco headquarters and not tabulated.

For many years appellee has maintained a public relations department, including its public safety work, its highway activities, and legislative activities. At its own expense, starting at the kindergarten level and up through the various grades of elementary schools and into high schools and colleges, appellee has sponsored, developed, prepared and distributed large quantities of materials for safety educational work. It sponsored and developed the idea of school safety patrols in 1923; it has published and furnished, free of charge, publications dealing with safe driving, driver training, and other subjects, and has prepared and distributed vast numbers of safety posters and safety lessons. Appellee has also established a traffic survey service available to communities without charge, and assists such communities in putting its recommendations into effect (R. 133, 202-208).

One of its important activities, and one included in its original Articles of Incorporation, has been the development and recommendation of adequate, sound, motor vehicle legislation, and sound and adequate highway improvement programs. It has sought appropriate legislation not only from the State legislature but from municipalities and counties as well (R. 208, 209).

Appellee has promoted a uniform traffic code for all cities within its territory. In 1943 and 1944, it sponsored the National Pedestrian Protection Contest. It has carried on weekly radio programs on safety work. It maintains a film library in connection with safety work and now has 23 films in its library available

without charge to anyone desiring to use such films on traffic safety. It has sponsored summer session courses at the University of California in driver education and driver training (R. 209-212).

Viewing all of the major activities of appellee as above outlined, as well as other activities referred to in testimony and in stipulated documentary evidence, it is obvious that all of these activities were designed and carried on for the purpose of contributing to the comfort, convenience, contentment, satisfaction, pleasure and recreation of appellee's members. Any legislative accomplishment which provides for the opening, extension or improvement of highways, or making driving conditions safer and less onerous for the owner of a pleasure car, contributes to the physical as well as mental wellbeing, pleasure and recreation of the member.

Likewise, it is clearly apparent that the numerous safety measures instituted and carried on by appellee directly aid and benefit its members by making motoring conditions less hazardous, thus importantly contributing to their comfort, ease of mind and safety.

It is interesting to note on page 12 of appellant's brief his admission that the members of appellee no doubt "find considerable satisfaction and comfort" in knowing that they will be towed to a garage if necessity requires, etc.

On page 13 of appellant's brief he admits that although "in an extremely remote way" the recreation of appellee's members is involved in its operations.

From the foregoing recital of activities and accomplishments it appears that appellee has kept fully abreast of the times and has enlarged and expanded its field of activities over the years since its organization to keep pace with constantly changing problems created by the ever-increasing density of automobile traffic, and particularly the greatly increased speed of automobiles with its attendant danger to both pedestrian and other vehicular traffic. Thus safety measures and education have played a prominent part in the program of appellee. Can it be doubted that successful efforts of such a nature contribute very materially to the enjoyment, contentment, well-being, satisfaction, and both physical and mental relaxation and recreation of appellee's members, for whose benefit such projects are undertaken? The fact that incidentally other automobilists and the general public are also benefited and educated does not detract in any sense from the pleasure and recreation of the members, rather it enhances the consequential benefits to them.

During 1943 and 1944, the opportunity for furnishing customary services to appellee's membership was to a considerable degree curtailed because of war-time restrictions, gasoline rationing, and the difficulty of obtaining both labor and materials for road signing and other work. In spite of that fact, appellee carried on its activities to the greatest extent possible, but also bent its energies to assist in war work within the scope of its field of endeavor, and furnished many services and benefits to persons connected with the prosecution of the war as well as to Federal Government Depart-

ments and Agencies, such as, for instance, the construction and erection of about 8,000 dimout signs. It furnished instruction in the training of drivers for the American Red Cross and the American Women's Volunteer Service.

It should be noted, that services benefiting persons, other than members of appellee, as well as services rendered to the Federal Government, the Red Cross, and other agencies during the war, were furnished without cost, so that there was no element of profit involved in the rendition of such services in 1943 and 1944, or in any other year.

In that connection, it should be pointed out that certain activities which would result in the receipt of very small amounts of income had been abandoned prior to the year 1943. For example, the finance department, described on page 5 of Exhibit 1-D, was abandoned about February, 1942. The rental of a frame building used as a garage and located on appellee's San Francisco property was abandoned in October, 1941. The appellee had also abandoned, prior to 1943, special memberships to hotels, garages and road service stations from which a small amount of income had theretofore been received and all advertising revenue from the publication of the monthly magazine "Motorland" had ceased late in 1941. Likewise, appellee had eliminated, prior to 1943, the very small amount of income received from sales of license plate frames.

The receipt of a small amount of incidental income is not, however, under the authority of a number of decided cases, sufficient to destroy the tax exempt status of clubs otherwise qualifying under Section 101(9) of the Internal Revenue Code. This has been held to be true even in some instances where the amounts of such income were quite large and were from sources entirely dissociated from the main purpose of the club. The Supreme Court of the United States in *Trinidad v. Sagrada Orden,* 263 U. S. 578, pointed out, in a case arising under a somewhat similar provision of law, that the statute says nothing about the *source* of the income but makes its *destination* the ultimate test of exemption. That principle of law has been cited and followed by a number of Federal courts in cases involving the application of Section 101(9) of the code. In his affidavit of October 5, 1941 (Exhibit 1-D), Mr. Watkins made the following statement:

> "*Disposition of Income:* The entire income of the Association is used to carry out the purposes recited in its Articles of Incorporation and to render to its members the various services previously enumerated. No distribution of income has ever been made to members nor does any profit inure to the benefit of any individuals."

The testimony and exhibits in this case show that such statement was also true in 1943 and 1944, although war services were rendered to Governmental and other agencies, but the rendition of such services

would clearly qualify under the phrase in Section 101(9), "other non-profitable purposes".

One of the outstanding cases in the Federal Courts dealing with the exact question of the tax exempt status of certain corporations under Section 101(9) and other similar sub-sections, is *Koon Kreek Klub v. Thomas, et al,* 106 Fed. (2d) 616, decided by the Fifth Circuit Court of Appeals. In that case the appellant was organized as a fishing and hunting club, maintaining a clubhouse, boats, and fishing and game preserves for the pleasure and amusement of its members, and it acquired a tract of land containing 6,777 acres, which completely surrounded a tract of 340 acres owned and occupied by one Thomas. It granted grazing privileges to Thomas for a consideration of $500 per year, and for a certain period extended similar privileges to its manager for $100 per year. Prior to the tax years before the Court, the club received income from dues which averaged $12,500 per year. Oil was later discovered about seven miles from the club property and in 1934, one of the years under consideration, the club granted an oil lease on its entire property at a rate of $4.00 per acre, with an annual renewal rental of $1.00 per acre, reserving the usual royalties. The lease was not renewed, however, and the amount received, which exceeded $25,000, was used to reduce or retire a mortgage which had been outstanding against the property since its acquisition by the club.

The Court found that the question of tax liability turned upon the interpretation of Section 101(9) of

the Revenue Act of 1934 (identical in 1943 and 1944), and held that whatever financial gain was realized from the grazing and leasing activities was incidental to and directed toward the accomplishment of the purpose upon which the income tax exemption was based.

The Court continued:

"The contention that the club did not operate exclusively for non-profitable purposes because of the leases of grazing rights is equally without foundation. In order to maintain its houses and preserves, it was required to raise funds from some source. That these funds might be derived from a use of the properties themselves, *not inconsistent with the purposes for which they were maintained, would not change the nature of the operation any more than an increase in dues charged to members. Indeed, if the club could be made self-sustaining by grazing fees, guest fees and other prerequisites, its operations being for the stated purposes, its exempt status would not be affected.* We need but to extend this principle to the acquisition of the preserves themselves to demonstrate that the granting of oil leases to obtain money with which to pay the mortgage debt did not change the character of the organization.

* * * * * * *

"We think the question is controlled by the decision *in Trinidad v. Sagrada Orden, 263 U. S. 578, 44 S. Ct. 204, 68 L. Ed. 458, wherein the court points out that the statute says nothing about the source of the income, but makes its destination the ultimate test of exemption.* The act here involved provides exemption for 'clubs organized

> and operated exclusively for pleasure, recreation, and other non-profitable purposes, no part of the net earnings of which inures to the benefit of any private shareholder', while the statute before the Supreme Court provided exemption for corporations 'organized and operated exclusively for religious, charitable, scientific or educational purposes, no part of the net earnings of which inures to the benefit of any private stockholder or individual'. *The necessity of having money to carry on the enterprise, whether charitable or recreational, is present in both cases. Deriving funds from the properties owned to further either of these ends would be no more a departure in one case than in the other.*" (Italics supplied.)

Likewise, it was held in *The Goldsby King Memorial Hospital, a Corporation v. Commissioner,* CCH Dec. 14042 (M) that a corporation otherwise exempt is not deprived of exemption because it incidentally carries on a profitable activity in furtherance of its predominant charitable purpose.

See also *Anderson Country Club, Inc. v. Commissioner of Internal Revenue,* 2 T. C. 1238, *Santee Club v. White,* 87 Fed. (2) 5, *Town and Country Club v. Commissioner* (CCH Dec. 12924-A, December 30, 1942), *Roche's Beach, Inc. v. Commissioner of Internal Revenue,* 96 Fed. (2) 776, *Schofield v. Corpus Christi Golf and Country Club,* 127 Fed. (2) 452.

In the latter case, where the club had executed an oil lease on its property and received very substantial sums as royalties and bonus under the lease, the Court said:

"The statute expressly gives the exemption to clubs operated as this one was and as long as the exemption holds, all revenues of the club without regard to their source, are exempt from tax, *because under the statute it is the nature and character of the operations of the club and the use made of the revenues, and not their source, which determines the exemptions.* The judgment was right. It is affirmed." (Italics supplied.)

In *Forest Lawn Memorial Park Association, Inc. v. Commissioner of Internal Revenue,* 45 B.T.A. 1091, the Board of Tax Appeals held the petitioner corporation, which operated a cemetery for non-profit purposes, exempt from taxation under Section 101(5) of the Revenue Acts of 1934 and 1936, which granted exemption to cemetery companies owned and operated exclusively for the benefit of their members or which are not operated for profit, etc. In that case, in addition to the usual functions of a cemetery, the corporation sold flowers, booklets, postcards, brochures, etc., and wedding ceremonies were conducted in the two churches within the cemetery without charge except for services.

The Tax Court of the United States (formerly the Board of Tax Appeals) considered for the second time, involving later years, the Commissioner's repeated assertion that the petitioner was not entitled to exemption under the same statutory provisions, and the Court's decision was rendered in the second case in *Forest Lawn Memorial Park Association, Inc. v. Commissioner of Internal Revenue,* 5 T.C.M. 738. The

Government's claim in the second case was based on (1) the incidental activities of petitioner and the profitable operation of the corporation, and (2) the close connection between the corporation and the manager's family and holding company.

In granting exemption for the second time, the Tax Court said:

> "In presenting his case upon the merits respondent is confronted at the outset with the difficult task of successfully distinguishing this case from our prior decision. His contentions in the two cases are from necessity much the same. * * * * * * * * * * *
>
> "It is true that petitioner operated Forest Lawn at a profit, but it cannot be said that it was a cemetery company organized or operated *for* profit. On the contrary it was organized as a non-profit cemetery company and it has made no distribution of profits to its members. Its predominant purpose, as we said in our prior opinion was 'to operate and maintain a cemetery for the interment of the dead.' 45 B.T.A. 1091, 1100. *No additional fact is presented or change in charter or by-law urged to show that petitioner has changed its predominant purpose during the taxable years. We can find no new or different activities on the part of petitioner which might indicate a change in its predominant purpose. It is our opinion, therefore, that petitioner continued during the taxable years to be a non-profit cemetery company and that any profit resulting from its sales and services was incidental to its primary function of operating and maintaining a cemetery for the interment of the dead.* * * *" (Italics supplied.)

The Commissioner of Internal Revenue has not appealed the foregoing decision.

At the top of page 7 of appellant's brief the word "similar" has been bracketed in the quotation from the statute, and the quotation has been followed by the parenthetical statement "Italics supplied". We wish to make it clear that the word "similar" does not appear in the statute itself but has also been supplied.

On pages 12 and 13 appellant argues that appellee was not organized and operated exclusively for pleasure or recreation and that the words of the statute "and other non-profitable purposes" do not, under the rule of *ejusdem generis,* enlarge the meaning of the preceding words of the statute. The interpretation for which appellant contends would make the phrase "and other non-profitable purposes" quite meaningless and would violate the well established rule that every word in a statute is to be given some meaning. The use of the conjunction "and" shows quite clearly that Congress did intend to expand the category of exempt clubs. If appellant's contention were to be conceded the statute might well have read "clubs organized and operated exclusively for pleasure and recreation, no part of the net earnings of which inures to the benefit of any private shareholder".

The rule of *ejusdem generis* is not of universal application but is only a rule of interpretation and is subject to qualification. One such qualification is that meaning must be given to the general words on the assumption that Congress intended them to mean

something more and in addition to the specific words. The rule clearly is not to be applied to the extent of making the general words meaningless. In this connection it is worthy of note that while Section 101 of the Internal Revenue Code includes 19 subsections, the one with which we are here concerned, (9) is the only one of the 19 where specific words are followed by the phrase "and other non-profitable purposes."

The introductory language in Section 101 states that "The following organizations shall be exempt from taxation under this chapter * * *." Thus we start out with a broad classification in the statute followed by an enumeration of 19 kinds of organizations to which exemption has been granted.

An examination of Section 101(12), for example, shows that Congress knows how to limit general words in tax exemption statutes when a limitation is intended. In that section the expression "or like associations" is the limiting language, and is, in essence, what the Government is asking the Court in this case to read into subsection (9). We believe that if Congress had intended such a limitation in subsection (9) it would have inserted one as it did in subsection (12).

Section 101(8) extends exemption to "Civic leagues or organizations not organized for profit, but operated exclusively for the promotion of social welfare * * *" and under this subsection the *Pickwick Electric Membership Corporation* has been held exempt in 158 Fed. (2d) 272, although that corporation obviously is not a civic league in any sense of the word but does qualify

as an organization not organized for profit and operated exclusively for the promotion of social welfare. This would indicate that the use of general language such as "organizations organized for profit" following more specific words such as "Civic leagues" is not to be strictly limited by the specific words.

Indeed, there is evidence that the Government itself considers the phrase "and other non-profitable purposes" as a general description of clubs to be granted exemption under subsection (9), as is evidenced by the ruling in G.C.M. 22116, 1940-2 C.B. 100, infra, in which the M Alumni Association was exempt from tax under Section 101(9), and in I.T. 2693, XII-1 C.B. 59, infra, where tax exemption was allowed a club incorporated for the purpose of making roads and trails in certain mountains, "to erect camps and shelter houses therein, to furnish maps and guidebooks thereof, and in other ways to make these mountains play a larger part in the life of the people."

The Supreme Court of the United States had occasion to consider the rule of *ejusdem generis* and the limitations thereon in *Helvering, Commissioner of Internal Revenue v. Stockholms Enskilda Bank,* 293 U.S. 84, 79 L. Ed. 211, where it said:

> "But it is said that the phrase in question must be restricted in accordance with the rule of ejusdem generis. The point is not without merit. The phrase reads 'interest on bonds, notes, or other interest-bearing obligations.' If the rule invoked be held controlling, it would follow that the general words 'other interest-bearing obliga-

> tions' must be assimilated to the particular words 'notes and bonds,' and restricted to obligations of the same kind. But while the rule is a well-established and useful one, it is like other canons of statutory construction, only an aid to the ascertainment of the true meaning of the statute. It is neither final nor exclusive. To ascertain the meaning of the words of a statute, they may be submitted to the test of all appropriate canons of statutory construction, of which the rule of ejusdem generis is only one. If, upon a consideration of the context and the objects sought to be attained and of the act as a whole, it adequately appears that the general words were not used in the restricted sense suggested by the rule, we must give effect to the conclusion afforded by the wider view in order that the will of the legislature shall not fail."

In *State of Texas et al. v. United States et al.,* 6 F. Supp. 63, p. 65, the Court said:

> "First of all, the rule ejusdem generis is a rule of construction only 'to be used as an aid in the ascertainment of the intention of the lawmakers, and not for the purpose of subverting such intention when ascertained.' *Mid-Northern Oil Co. v. Walker,* 268 U.S. 45, 49, 45 S. Ct. 440, 441, 69 L. Ed. 841."

Appellant, on page 13 of his brief, says that in interpreting a similar statute, referring to Section 101(9) of the Code, the Court in *Better Business Bureau v. United States,* 326 U.S. 279, held that the word "exclusive" in the statute meant just what it said and is not to be interpreted otherwise. We cannot

agree that the Court made any such holding in that case. The question there involved was whether the Better Business Bureau of Washington, D. C., was entitled to exemption from social security taxes as a corporation organized and operated exclusively for scientific or educational purposes within the meaning of Section 811(b)(8) of the Social Security Act. In the course of its discussion the Court made the following statement:

> "In this instance, in order to fall within the claimed exemption, an organization must be devoted to educational purposes exclusively. This plainly means that the presence of a single non-educational purpose, *if substantial in nature,* will destroy the exemption regardless of the number or importance of truly educational purposes." (Italics supplied.)

The above modification "if substantial in nature" does not accord with appellant's interpretation as set forth in his brief but, on the contrary, is in accord with the earlier holding of the Supreme Court in *Trinidad v. Sagrada Orden,* infra, which likewise permitted departure from a strict and literal construction of the term "exclusive", and has been cited by many Courts to emphasize such departure. A few such decisions have already herein been discussed or cited. The *Sagrada Orden* case dealt with a statute exempting corporations from income tax if organized and operated "exclusively" for religious, charitable, scientific or educational purposes, no part of whose net income inures to the benefit of any individual.

The qualifying phrase above referred to in the *Better Business Bureau* decision "if substantial in nature" is, of course, of the utmost importance and permits a taxpayer to engage, to a limited extent, in activities beyond the strict scope of the purposes enumerated in such tax-exempting provisions as Section 101(6), considered in the *Better Business Bureau* case, and Section 101(9) here involved.

On page 14 of his brief, appellant contends that a golf, rod or gun club may be income tax exempt under the section here involved, but the automobile club is a different type of organization and believes that most anyone, "including members of Congress", would think so. Assuming, *arguendo,* that may be so, it by no means follows that both types of clubs may not be tax exempt under Section 101(9). There is no language in Section 101(9) which limits exemption to golf, rod, gun and similar clubs, nor, indeed, has the Bureau of Internal Revenue itself limited such exemption to the type of club described by appellant. See, for example, G.C.M. 22116 and I.T. 2693, infra.

Appellant also, on page 14, states that this case is quite obviously important from a revenue standpoint. We respectfully submit that its asserted importance from such a standpoint is no reason for denying tax exemption, and we are confident that the Court will consider and decide this case only upon its merits. Also, if the Government means that an affirmation by this Court of the judgment of the lower Court means that the overall revenues of the Government will be seriously affected, we believe such a contention to be

wholly untenable, in view of the vast tax revenue collected by the Government each year as compared with the very limited number of automobile clubs throughout the United States, and their insignificant effect upon the revenues, even if all of them were able to qualify for exemption under Section 101(9).

D. NO PART OF THE NET EARNINGS OF APPELLEE HAS EVER INURED TO THE BENEFIT OF ANY PRIVATE SHAREHOLDER OR MEMBER.

No stock has ever been issued to members of appellee and it has never paid dividends of any nature to any member. None of its income has ever been paid or credited to any member on its books, no provisions have ever been made to pay or to credit any net earnings to its members, nor has appellee any plan or purpose to distribute its net earnings so as to inure to the benefit of any individual member. Further, no director of appellee nor any officer, as such, received any salary or other compensation in 1943 or 1944.

The amendment of Article VI of the original Articles of Incorporation points out (Exhibit 1-B):

> "That said Corporation is not organized for pecuniary profit * * *."

As previously stated, the entire income of the appellee is normally used to carry out the purposes for which it was incorporated and to render to its members the various services hereinbefore outlined. The amounts so expended were, however, below normal in

1943 and 1944 as in those years appellee was rendering services connected with the war effort, and in addition had to economize on both labor and materials, both of which were difficult to obtain, so that wartime restrictions, as found by the Court below, prevented it from expending all its annual receipts in 1943 and 1944.

In *Koon Kreek Klub v. Thomas, et al.,* infra, the Court said that so long as profits "are retained by the organization or used to further the purposes which are made the basis of exemption and are not otherwise used for the benefit of any private shareholder * * *," such profit cannot be deemed to inure to the benefit of any private shareholder.

Appellee's Exhibit 4, entitled "Composition of Surplus Balance", covers the period annually from December 31, 1931 to December 31, 1946, together with the first quarter of 1947, representing an analysis of appellee's surplus account taken from its records. This statement, in the third column, shows the amount of the unexpended income after taking out the amount of unearned dues for each year beginning December 31, 1937, down to and including March 31, 1947. That column shows an excess of $7,868.71 at December 31, 1937, which changed into a deficiency in 1938 and continued in 1939 and 1940. During the next five years, the income exceeded the expenses and as a result there was a surplus balance for those years. In 1946, the expenditures exceeded the income, resulting again in a deficiency, and there was also a deficiency for the first quarter of 1947.

The fifth column shows that for the sixteen years included in said statement, eight years were in the black and eight years in the red. Consequently, in some years appellee took in more than it spent, and in others spent more than it received during the year.

We believe it is clear that no part of appellee's net earnings has inured to the benefit of any member, and that it was never intended that they should.

E. DUE REGARD MUST BE GIVEN TO THE OPPORTUNITY OF THE TRIAL COURT TO JUDGE THE CREDIBILITY OF THE WITNESSES AND TO VIEW THE EVIDENCE.

The only evidence adduced in the Court below was the oral testimony of witnesses offered by appellee together with documentary evidence. No witnesses were offered on behalf of appellant.

Rule (52(a) of the Rules of Civil Procedure for the District Courts of the United States provides in part:

> "Findings of fact shall not be set aside unless clearly erroneous, and due regard shall be given to the opportunity of the trial court to judge the credibility of the witnesses."

In *Wittmayer v. United States,* 118 Fed. (2d) 808, 811 (C.C.A. 9th), this Court stated in interpreting Rule 52(a) that:

> "The provisions of the new procedural rules that the findings of fact of the trial judge are to be accepted on appeal unless clearly wrong (Rule 52(a), 28 U.S.C.A. following Section 723c), is but the formulation of a rule long recognized and ap-

plied by courts of equity. *Guilford Const. Co. v. Biggs,* 4 Cir., 102 F. (2d) 46, 47.

"As was said by Mr. Justice Holmes in *Adamson v. Gilliland,* 242 U.S. 350, 353, 37 S. Ct. 169, 170, 61 L. Ed. 356 (citing *Davis v. Schwartz,* 155 U.S. 631, 636, 15 S. Ct. 237, 39 L. Ed. 289), the case is pre-eminently one for the application of the practical rule, that so far as the findings of the trial judge who saw the witnesses 'depends upon conflicting testimony or upon the credibility of witnesses, or so far as there is any testimony consistent with the finding, it must be treated as unassailable.' "

Similarly, in *United States v. Aluminum Co. of America,* 148 F. (2d) 416, 433, the Court of Appeals for the Second Circuit held that when a trial judge has seen the witnesses:

"* * * and in so far as his findings depend upon whether they spoke the truth, the accepted rule is that they 'must be treated as unassailable.' *Davis v. Schwartz,* 155 U.S. 631, 636, 15 S. Ct. 237, 39 L. Ed. 289; *Adamson v. Gilliland,* 242 U.S. 350, 353, 37 S. Ct. 169, 61 L. Ed. 356; *Alabama Power Co. v. Ickes,* 302 U.S. 464, 477, 58 S. Ct. 300, 82 L. Ed. 374. * * *; and upon an issue like the witness's own intent, as to which he alone can testify, the finding is indeed 'unassailable,' except in the most exceptional cases."

In the light of the foregoing interpretations by this Court, as well as by the Second Circuit Court of Appeals, in the cases cited, attention is again invited to the findings of the lower Court in the case at bar, particularly the following:

"That the sum total of the activities of the Plaintiff is designed to alleviate the occasional hardships and inconveniences which are connected with the ownership and operation of pleasure automobiles, and the services rendered by Plaintiff are for the pleasure and recreation of its members (R. 84)."

"That none of the normal activities or the wartime activities of the Plaintiff were conducted for the purpose of earning a profit or accumulating a surplus, nor was any profit derived from any of these activities (R. 84-85)."

"It has been the policy of the Plaintiff to expend on services all its annual receipts, and during 1943 and 1944 it was prevented from so doing only by reason of wartime restrictions. That in the 16-year period from and including 1931 to 1946 the Plaintiff has had a deficit in 8 years and a surplus in 8 other years (R. 85)."

"That the Plaintiff has never distributed, set aside, or credited on its books by way of dividends or from its earnings any money to any of its members as an incident of their membership in the Plaintiff association. That there has never been any intention to distribute any net income direct to the members. That the directors of Plaintiff serve without financial remuneration (R. 85)."

"That the Plaintiff has only the powers necessary to carry out its purposes. The Plaintiff has no power to distribute or set aside any portion of its net income to its members or to any other person except to carry out its purposes (R. 83)."

"That the Plaintiff is a continuing organization whose members make common cause both in

a financial sense and in carrying out its stated purposes by group activity as well as by individual action (R. 85)."

"That Plaintiff association is a club (R. 86)."

Consequently we believe that the foregoing findings, together with other findings of the trial Court, conclusively show that appellee fully meets the requirements of Section 101(9) of the Internal Revenue Code, and that such findings, in the language of *Wittmayer v. United States, supra,* must in the language of this Court, "be treated as unassailable".

CONCLUSION.

The judgment of the District Court was correct and should be affirmed.

Dated, San Francisco, California,
January 26, 1949.

Respectfully submitted,
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